AF1 Income Tax 2023/24
Part 4: Adjusted Net Income

This part will introduce two further situations that could be part of a calculation question:

- The reduction in the Personal Allowance for high earners
- The High Income Child Benefit Tax charge

In both cases we need to calculate the subject's **adjusted net income (ANI)**.

The milestones are:

- To be able to calculate adjusted net income.
- To apply this correctly to a reduction in the subject's personal allowance
- To be able to calculate the High Income Child Benefit tax charge.

Calculating an individual's ANI

Most people would consider net income to be their income after tax but HMRC have a different definition!

The starting point is to total all the individual's taxable income. This will include all non-savings, savings and dividend income together with chargeable gains under non-qualifying life policies. Do not deduct the PA. Tax free income such as from ISAs are excluded.

You then deduct.

- Pension contributions which have been paid gross into an **occupational scheme**
- Trading losses.(if self-employed)

This figure is what HMRC classify as net income.

You then deduct:

- Grossed up contributions to Personal Pensions (net contribution divided by 0.8)
- Grossed up Gift Aid contributions. (net gift divided by 0.8)

The resultant figure is the **adjusted net income**.

David has a gross income of £50,000 and contributes 5% (£2,500) to his employer's OPS. In addition he receives dividends totalling £20,000. He pays £10,000 (£12,500 gross) into his Personal Pension and a Gift Aid contribution of £1,000. (£1,250 gross)

His ANI is £70,000 less (£2,500 + £12,500 + £1,250)= £53,750

ANI is significant in three situations:

- if ANI is over £100,000 the PA is reduced
- Establishing the amount of an individual's PSA
- if ANI is more than £50,000 a child benefit tax charge is made

Withdrawal of Personal Allowance

If an individual's Adjusted Net Income (ANI) exceeds £100,000 their personal allowance is reduced by £1 for each £2 of income above this. Personal Allowance is lost completely once ANI exceeds £125,140. (£100,000 + £12,570 x 2). The marginal rate of tax between £100,000 and this figure is effectively 60%.

Jane's salary is £100,000 and is awarded a £10,000 bonus. Tax is payable at 40% on the bonus but it reduces her PA by £5,000 so this becomes subject to tax at 40%. Her total liability is £6,000 which is 60% of the bonus.

£125,140 is also the threshold where an individual starts to pay tax at the additional rate. However as the PA is reduced when ANI is more than £100K, it's not correct to state that you only pay additional rate tax if total income is more than £137,710 (£12,570 +£125,140)

You don't need to calculate an individual's ANI in every question but if the total income is above or seems to be approaching £100,000, it should be the first step of the calculation.

Mary has a basic salary of £115,000. She made a net PP contribution of £4,000 and a donation using Gift Aid of £800.

In calculating Mary's income tax liability:

The first step is to calculate her ANI and reduced PSA.
ANI is £115,000 less (£5,000 + £1,000) = £109,000
Her PA is reduced by £4,500 (£9,000/2) to £8,070

Besides reducing her ANI, the PP and Gift Aid will extend her higher and additional rate thresholds.

Her higher rate threshold is increased to £43,700 (£37,700 + £6,000)
Her additional rate threshold is increased to £131,140 (£125,140 + £6,000)

Her liability is:

£8,070 @ 0%	0
£43,700 @ 20%	£8,740
£63,230 @ 40%	£25,292
£115,000	£34,032

In this example there is also savings and dividend income.

Phil has a salary of £108,000. In addition he has savings income of £6,000 and Dividend income of £20,000.

He also contributes £18,000 into a SIPP

His total income is £108,000 + £6,000 + £20,000 = £134,000.
His ANI is £134,000 sess £22,500 (£18,000/0.8) = £111,500

£11,500/2 = £5,750
PA is £12,570 less £5,750 = £6,820
His higher rate threshold is £37,700 + £22,500 = £60,200
His additional rate threshold is £125,140 + £22,500 = £147,640

Non-Savings Income

£6,820 @ 0% =	0
£60,200 @ 20% =	£12,040
£40,980 @ 40% =	£16,392

Savings income

£500 (PSA) 0%	0
£5,500 @ 40%	£2,200

Dividend Income

£1,000 @0%	0
£19,000 @ 33.75%	£6,412.50
	37,044.50

Note that none of his income is in the additional rate band and therefore he gets a PSA of £500.

If he hadn’t made the SIPP contribution his ANI would be £134,000 and he would have no PA. Nor would he benefit from the extended higher and additional rate thresholds.
His liability would be:

<u>Non-Savings</u>

£37,700 @ 20% =	£7,540
<u>£70,300</u> @40% =	£28,120
£108,000	

<u>Savings</u>

£6,000 @ 40% £2,400 (no PSA as his taxable income is more than £125,140)

<u>Dividend</u>

£1,000 @0%	0
£10,140 @ 33.75%	£3,422.25
<u>£8,860</u> @39.35%	<u>£3,486.41</u>
£20,000	£44,968.66

ANI and the PSA.

The test for how much PSA an individual gets depends on their ANI.

- In the last example no pension contributions were made and the ANI is £134,000.
- As he has no PA then £8,860 (£134,000 less £125,140) is in the additional rate band so he has no PSA.
- In the previous example where pensions contributions have been made the ANI was £111,500.
- The higher rate threshold was extended to £147,640 therefore there is no income in the additional tax band so he gets a PSA of £500

ANI is also used to check whether the income threshold for Married Couples Allowance has been exceeded.

Whilst the taxation of chargeable events under an Insurance Bond will be covered in more detail the Taxation of Investments, when a CE occurs, the whole gain forms part of the individuals ANI

Helen has a pension income of £30,000. In 23/24 she surrendered an IB giving a gain of £100,000.

Her ANI is £130,000 so he has no PA for that tax year and all her pension income will be taxed at 20%

Here's a final example of a calculation using ANI

Paul has a salary of £180,000. He pays £20,000 to a group of charities claiming Gift Aid. He gets £3,000 in interest and £40,000 in dividends

Salary	£180,000
Interest	3,000
Dividends	40,000
	£223,000
Less Gross Gift Aid	25,000
	£198,000

He has no PA but both the higher rate and additional rate thresholds are extended to £62,700 and £150,140. The higher rate band will be £87,440 (£150,140 less £62,700) He will be in the additional rate band so his PSA is nil

Non savings	£62,700 @20%	£12,540
	£87,440 @ 40%	£34,976
	£29,860 @ 45%	£13,347
Savings	£3,000 @ 45%	£1,350
Dividends	£1,000 @ 0%	
	£39,000 @ 39.3%	£15,346.50
Total		**£77,559.50**

High Income Child Benefit tax charge

When it was first introduced Child Benefit was universal and tax free. Since 2013-14 it has been restricted if one individual in the family has an adjusted net income of greater than £50,000.

The basic rules are:

- If ANI is higher than £50,000 the individual must register for self assessment.
- If one person in the household has an ANI greater than £60,000 child benefit is withdrawn. The family can choose whether to give this up completely or to still collect it and pay the high income tax charge
- If ANI is between £50,000 and £60,000 the benefit is still paid but there is a tapered tax charge

The higher earner needn't be the child's parent or guardian nor in a married relationship.

Paula has earnings of £25,000. She has one child and qualifies for full Child Benefit. She meets Emile and starts to live with him. His ANI is £65,000 so Paula will either have to give up child benefit or Emile will have to pay the full tax charge.

For 2023/24 Child Benefit is paid at a rate of £24.00 for the first child and £15.90 for subsequent children. (These figures are in the exam tax tables)

Child Benefit as with almost all social security benefits is quoted on a weekly basis but is normally paid on a four weekly basis. In a calculation question just multiply the weekly amount by 52. The annual amounts are:

One child	£1,248
Two children	£2,074.80
Three children	£2,901.60

If one income is over £50,000 then there is a tax charge of 1% of the family's child benefit for every complete £100 or income exceeds £50,000. Note that this means no tax charge is made until ANI is more than £50,099 since it is a 1% reduction for every complete £100

William and Kate have two children and their Child Benefit is £39.90 a week which on an annual basis is £2,074.80

Kate has an income of £52,340 so she has to pay a tax charge of 23% of the total Child Benefit which would be £477 (The tax charge is rounded down and pence are ignored)

Once income is £60,000 the charge will equal the amount of child benefit so these individual can elect not to receive child benefit.

Paying the charge

- The highest earner must register for self-assessment
- Declare the amount of Child Benefit
- Declare their ANI

Stephanie has two children and earns a salary of £56,000. She receives £2,074.80 in child benefit. All other income is in her partner's name as he is a non-taxpayer. She contributes £300 a month into her SIPP. Calculate her tax liability including any child benefit tax charge.

Salary	£56,000
Less PA	£12,570
	£43,430

Basic rate band extended by gross SIPP contribution to £42,200 (£300 x 12 = £3,600/0.8 = £4,500)

£42,200 @ 20%	£8,440
£1,230 @ 40%	£493
Total	£8,993

Child Benefit tax charge

Salary	£56,000
Less gross SIPP	£4,500
ANI	£51,500
Less	£50,000
	£1,500
£1,500/100 = 15	
£2,074.80 x 15%	£311 (figure rounded down)

You should now understand

- To be able to calculate adjusted net income.
- To apply this correctly to a reduction in the subject's personal allowance
- To be able to calculate the child benefit tax charge.

Sources

https://www.gov.uk/guidance/adjusted-net-income

https://www.gov.uk/child-benefit-tax-charge